

This record is a partial extract of the original cable. The full text of the original cable is not available.

UNCLAS BRASILIA 002546

SIPDIS

NSC FOR WALLACE  
TREASURY FOR SSEGAL  
PLS PASS FED BOARD OF GOVERNORS FOR WILSON, ROBATAILLE  
USDA FOR FAS/FAA/ITP  
USDOC FOR 4322/ITA/IEP/WH/OLAC-SC

E.O. 12958: N/A

TAGS: [EFIN](#) [ECON](#) [EINV](#) [PGOV](#) [BR](#)

SUBJECT: Central Bank Eases Reserve Requirement

11. The Central Bank (CB) on Friday August 8 reduced its reserve requirement on banks' demand deposits from 60 to 45%. That requirement thus reverts to what had been its long-term level from June 2000 until the CB raised it in February of this year, at the peak of Brazil's recent inflation uncertainties, in tandem with what was then the second successive monthly hike under the new GoB of the SELIC benchmark interest rate. (Prior to March 2000, the reserve requirement was actually higher, at 65%.) The change does not affect requirement on term deposits or savings accounts, which remain at 23 and 30%, respectively.

12. Effective August 11, this move will free up eight billion Reals (about USD 2.7 billion) for banks' use, according to the CB's Monetary Policy Department. The GoB hopes this money will be put to benign effect in the form of expanding credit and reducing interest rates. Brazil's three biggest national retail banks (Bradesco, Itau and Unibanco) have already announced modest adjustments of some retail interest rates -- from 9.3 and 9.35% to 8.7 and 8.9% per month (sic), respectively, on private check-credit rates by Bradesco and Itau, for example.

13. The drop had been universally awaited as a signal of the GoB's anti-recessionary resolution. However, no-one believes its direct effect will be anything more than marginal in fomenting economic revival. Numerous commentators note, in fact, that lack of demand for credit in Brazil's somber current economic landscape may result in the freed-up funds not going towards new loans at all, just into banks' purchases of more GoB bonds, or of foreign currency.

14. The CB announcement came against a background of ever-intensifying demands for GoB policies to stimulate growth, plus work on a vaguely-described GoB package of emergency measures (Septel). As token of the pressure, Chief of Staff Dirceu had earlier been quoted conspicuously out-of-portfolio as promising Brazil's governors that the reserve requirement would be lowered by week's end. Amidst some media reports that the decision was resisted by Central Bank professionals, Finance Minister Palocci has since made a point of stressing that it was made on purely technical, not political grounds, and was justified by positive developments in Brazil's inflation data and expectations.

15. A senior CB contact volunteered to us Friday afternoon that the reserve-requirement change's impact seemed to have been even more modest than the Monetary Policy Department had hoped, to judge from the early exchange-rate reaction. He implied further cuts in the rate might be considered, even though, at 45%, it is now as low as it has been for years.

16. COMMENT: Brazil's economic focus will now be fixed on the COPOM's (Monetary Policy Committee) next decision concerning the SELIC rate, at its monthly meeting on August

20. With figures for industrial production showing a sectoral recession already under way, and with recent inflation numbers at least slightly better than had been feared, clamor can only grow for the COPOM to chop the SELIC by more than the 1.5% (from its present 24.5%) that the market has already begun to anticipate. We expect the CB not/not to bend to ongoing public and political protests over the Lula administration's economic-policy course, but nor do those protests look likely to abate